

Generally, sales of "canned" computer software are taxable retail sales in Illinois. See 86 Ill. Adm. Code 130.1935. (This is a GIL.)

January 11, 1999

Dear Mr. Xxxxx:

This letter is in response to your letter dated December 1, 1998. The nature of your letter and the information you have provided require that we respond with a General Information Letter which is designed to provide general information, is not a statement of Department policy and is not binding on the Department. See 86 Ill. Adm. Code 1200.120(b) and (c), enclosed.

In your letter, you have stated and made inquiry as follows:

We have a service center in Illinois that has acquired computer software from an out-of-state vendor. Attached is a copy of our contract with the supplier. We are questioning if it is subject to sales or use tax because:

- a) it is not a 'sale at retail' or
- b) is it exempt under the Reg. 130.1935(a)(1)

As to point a, please refer to paragraph

- 1) 8.2.1 which indicates no title or ownership is transferred to the customer,
- 2) 8.1.2 which restricts our action with out the permission of the supplier
- 3) 8.2.3 which limits our ability to modify the software.
- 4) 6.1.4 requires us to return an software replaced under warranty

With respect to the about paragraphs we ask if title has transferred sufficiently to meet the requirement of a 'sale to retail'

With respect to point b, please refer to paragraph

- 1) 8.1.3 which limits our ability to make copies
- 2) 8.1.1 which limits our ability to sublicense
- 3) 8.9.3(e) which gives us a right to another copy if the original is unusable
- 4) While the contract is silent on disposition of the software once our license has expired, we feel the restrictions placed on us (unable to move to another computer, modify, transfer, or sell) indicates the seller expects the software back or expects us to destroy it after we are no longer using the software.

With respect to the second set of paragraphs we ask if this is exempt from sales tax as a 'license of software' under rReg. 130.935(a)(1)

Thank you for your time and help.

We are unable to give you the ruling you request in the context of a General Information Letter. The following general information is helpful in determining whether computer software is taxable.

Generally, sales of "canned" computer software are taxable retail sales in Illinois. See the enclosed copy of 86 Ill. Adm. Code 130.1935. However, if the computer software consists of custom computer programs, then the sales of such software may not be taxable retail sales. See Section 130.1935(c).

Custom computer programs or software are prepared to the special order of the customer. The selection of pre-written or canned programs assembled by vendors into software packages does not constitute custom software unless real and substantial changes are made to the programs or creation of program interfacing logic. See Section 130.1935(c)(3).

If transactions for the licensing of computer software meet all of the criteria provided in Section 130.1935(a)(1), neither the transfer of the software or the subsequent software updates will be subject to Retailers' Occupation Tax.

A license of software is not a taxable retail sale if:

- A) it is evidenced by a written agreement signed by the licensor and the customer;
- B) it restricts the customer's duplication and use of the software;
- C) it prohibits the customer from licensing, sublicensing or transferring the software to a third party (except to a related party);
- D) the vendor will provide another copy at minimal or no charge if the customer loses or damages the software; and
- E) the customer must destroy or return all copies of the software to the vendor at the end of the license period.

As stated above, licenses of computer software are not taxable if they meet all of the criteria listed in Section 130.1935(a)(1). However, item (D) of that part requires the license to contain a provision requiring the vendor to provide another copy at minimal or no charge if the customer loses or damages the software. The Department has deemed software license agreements to have met this criteria if the agreements do not contain a provision about the loss or damage of the software, but the vendors' records reflect that they have a policy of providing copies of software at minimal or no cost if the customers lose or destroy the software.

Item (E) of this part also requires a license to require a customer to destroy or return all copies of the software to the vendor at the end of the license period. The Department has also deemed perpetual license agreements to qualify for this criteria even though no provision is included in the agreements that requires the return or the destruction of the software.

I hope this information is helpful. The Department of Revenue maintains a Web site which can be accessed at www.revenue.state.il.us. If you have further questions related to the Illinois sales tax laws, please contact the Department's Taxpayer Information Division at (217) 782-3336.

If you are not under audit and you wish to obtain a binding Private Letter Ruling regarding your factual situation, please submit all of the information set out in items 1 through 8 of the enclosed copy of Section 1200.110(b).

Very truly yours,

Melanie A. Jarvis
Associate Counsel

MAJ:msk
Enc.